Office of Chief Counsel
Internal Revenue Service

memorandum

CC:WR:SCA:LN:GL-801742-00
WBDouglass

date:

to: Chief, Appeals Division, Southern California District,
Attention: Steve Millang, Appeals Officer, Riverside

from: District Counsel, Southern California District, Laguna Niguel
Willis B. Douglass, Attorney; Miriam A. Howe, ADC

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subject:

AOP on Whether Merits Should Be Considered in a CDP Case
Taxpayer: [redacted] **TIN** [redacted]

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By transmittal dated February 23, 2000, you requested our advice as to whether you should consider the underlying merits of the taxpayer's liability in the taxpayer's collection due process case. The memorandum is in response to your request.

ISSUES

(1) Does the IRS have the burden to show that a statutory notice of deficiency was received by the taxpayer?

(2) If the IRS cannot show that the taxpayer received a notice of deficiency, must Appeals address the merits of the underlying tax liability in the CDP hearing for this case?

(3) If Appeals considers the underlying merits of the tax liability in this case, must the IRS be able to prove how much unreported income the taxpayer earned during the years at issue?

CONCLUSIONS

(1) The statute, I.R.C. § 6330, is silent on the burden of proof on this issue. However, we believe that the IRS must at a minimum show that a notice of deficiency for the years at issue was mailed to the taxpayer's last known address.

(2) If the IRS cannot at least show that it mailed a notice of deficiency to the taxpayer's last known address, then at the CDP hearing, Appeals must consider the underlying merits of the tax liability.

(3) If the IRS can show sufficient predicate evidence, as discussed below, for its determination of income, then the notice of deficiency will be entitled to a presumption of correctness, and the burden of proof will be on the taxpayer to show that he did not receive the income set forth on the notice of deficiency. If the IRS cannot show sufficient predicate evidence to support the determination of unreported income on the notice of deficiency, the burden of proof on the unreported income issue shifts to the IRS.

FACTS

[redacted], the taxpayer, failed to file personal income tax returns for [redacted], [redacted] and [redacted]. TXMOD transcripts for these three years indicate that on [redacted], the IRS assessed deficiencies of $[redacted] for [redacted], $[redacted] for [redacted] and $[redacted] for [redacted] against the taxpayer. The TXMODs also show a Disposal Code 10 associated with each of these assessments. This indicates that the assessments were made as a result of a defaulted notice of deficiency. However, you have informed us that no examination files, certified mailing lists or other records beyond transcripts are available in this case. Therefore, the IRS has no records other than the transcripts to prove (1) that the notice or notices of deficiency were actually sent, (2) the address to which they were sent, and (3) whether the IRS received back any information indicating that the taxpayer did or did not receive the notices. Your transmittal states that "[i]t appears that all the audit assessments were based on Bureau of Labor Statistics. However, there is no certainty as to what the tax assessments are based on."

In response to your correspondence, the taxpayer claims that he did not work during the years at issue, had minimal income, and was not required to file returns for those years. The taxpayer claims that he lived with family and friends during the years at issue; however, the taxpayer has not provided the names and addresses of the persons with whom he lived.

You have submitted copies of an application ("rental application") dated [redacted], by which the taxpayer applied to rent an apartment. On the rental application, the taxpayer listed his employer from [redacted] to [redacted] as "[redacted]." He listed his supervisor as [redacted]. No area code was listed with the telephone number. No other information concerning the taxpayer's employment during the years at issue has been submitted to us.

You stated that you asked the taxpayer's representative whether or not the taxpayer received a notice (or notices) of deficiency for the years at issue. The taxpayer's representative has not answered this question. We too have attempted to contact the taxpayer's representative, but we have not been successful. Therefore, for purposes of this memorandum, we will assume that the taxpayer will deny having received a notice of deficiency for the years at issue, or he will state that he does not remember receiving such a notice.

ANALYSIS

The IRS Restructuring and Reform Act, P.L. 105-206, added § 6330 to the Internal Revenue Code. This statute is effective for collection actions taken after January 18, 1999. Under this new statute, the IRS is required to notify a taxpayer in writing at least thirty days prior to a proposed levy that the taxpayer may request a hearing before the IRS Office of Appeals to challenge the levy action. *See also* Temp. Treas. Reg. § 301.6330-1T(a)(1). If the taxpayer requests the hearing, the IRS may not levy on the taxpayer's property while the hearing is pending.

If the taxpayer requests a hearing under I.R.C. § 6330(a), the Appeals Officer holding the hearing must first verify that the requirements of any applicable law or administrative procedure have been met. I.R.C. § 6330(1). The taxpayer may then raise at the hearing any relevant issues, including appropriate spousal defenses, challenges to the appropriateness of collection actions; and offers of collection alternatives, including installment agreements and offers in compromise. I.R.C. § 6330(c)(2)(a).

The taxpayer may raise challenges to the underlying tax liability for any tax period if (1) the taxpayer did not receive a

notice of deficiency for that period, or (2) the taxpayer did not otherwise have an opportunity to dispute the tax liability in question. I.R.C. § 6330(c)(2)(B). Concerning this issue, the regulations provide as follows:

> Q-E2. When is a taxpayer entitled to challenge the existence or amount of the tax liability specified in the CDP Notice?
>
> A-E2. A taxpayer is entitled to challenge the existence or amount of the tax liability specified in the CDP Notice if the taxpayer did not receive a statutory notice of deficiency for such liability or did not otherwise have an opportunity to dispute such liability. Receipt of a statutory notice of deficiency for this purpose means receipt in time to petition the Tax Court for a redetermination of the deficiency asserted in the notice of deficiency. An opportunity to dispute a liability includes a prior opportunity for a conference with Appeals that was offered either before or after the assessment of the liability.

Temp. Treas. Reg. § 301.6330-1T(e)(3), Q & A E2.

> (4) *Examples.* The following examples illustrate the principles of this paragraph (e).
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> *Example 1.* The IRS sends a statutory notice of deficiency to the taxpayer at his last known address asserting a deficiency for the tax year 1995. The taxpayer receives the notice of deficiency in time to petition the Tax Court for a redetermination of the asserted deficiency. The taxpayer does not timely file a petition with the Tax Court. The taxpayer is therefore precluded from challenging the existence or amount of the tax liability in a subsequent CDP hearing.
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> *Example 2.* Same facts as in *Example 1*, except the taxpayer does not receive the notice of deficiency in time to petition the Tax Court. The taxpayer is not, therefore, precluded from challenging the existence or amount of the tax liability in a subsequent CDP hearing.

Temp. Treas. Reg. § 301.6330-1T(e)(4).

If the taxpayer is entitled to raise issues concerning underlying merits of the tax liability, the Appeals Officer must consider those issues at the hearing. I.R.C. § 6330(c)(3)(B).

For Tax Court cases dealing with determinations of deficiencies, I.R.C. § 6212(b) provides that an otherwise valid notice of deficiency is sufficient if it is mailed to the taxpayer's last known address. This applies regardless of whether or not the taxpayer actually receives the notice. However, for purposes of determining whether or not a taxpayer may contest the underlying merits of a tax liability in a CDP case, the issue is whether the taxpayer *received* the notice of deficiency, not simply whether the notice of deficiency was sent to the taxpayer's last known address. I.R.C. § 6330(c)(2)(B).

The term *last known address* is not defined by statute or current regulations. However, case law defines *last known address* as the "address which appears on the taxpayer's most recently filed return, unless [the IRS] has been given clear and concise notification of a different address." Abeles v. Commissioner, 91 T.C. 1019, 1035 (1988). The taxpayer's most recently filed return for this purpose is the last return filed by the taxpayer from which, if the return was properly processed, the address on the return was available to the IRS agent mailing a notice of deficiency. Id., at 1035. The IRS is in the process of promulgating new regulations concerning the definition of the term *last known address*, but they will not affect whether the notice(s) of deficiency at issue in the present case were sent to the taxpayer's last know address as that term was defined by Abeles, supra.

We believe that, for purposes of I.R.C. § 6330(c)(2)(B), a court will hold that a taxpayer is presumed to have received a notice of deficiency if the notice was sent to the taxpayer's last known address as defined above. We further believe that a court will allow a taxpayer to overcome this presumption with positive evidence that the taxpayer did not receive the notice of deficiency. For example, evidence that the taxpayer did not reside at the address to which the notice was sent would tend to show that the taxpayer did not receive the notice. In addition, if IRS records show that the notice of deficiency was returned because it was undeliverable, the taxpayer should prevail unless the taxpayer affirmatively refused to accept delivery of the notice of deficiency.

The primary problem in the present case is that the IRS has no records to show to what address the notice(s) of deficiency

was(were) sent. We believe that a mere transcript entry that a notice of deficiency was sent and that the taxpayer defaulted on the notice is insufficient to show, under I.R.C. § 6330(c)(2)(B), that the taxpayer *received* a notice of deficiency. Therefore, we believe that Appeals should consider the underlying merits of the tax liability in the present case.

In considering the underlying merits of the assessments made against the taxpayer for [redacted], [redacted] and [redacted], the IRS is again hampered by the fact that no files can be located which document how the IRS arrived at the deficiencies that were assessed. As noted above, you indicated that it is probable that Bureau of Labor Statistics were used to determine the taxpayer's income for the years at issue, but you also noted that we cannot be sure of this.

A notice of deficiency is ordinarily presumed to be correct, and the burden of proof is on the taxpayer to prove that the IRS's determination is incorrect[1]. Greenberg's Express, Inc. v. Commissioner, 62 T.C. 324 (1974). It is permissible to determine amounts of unreported income based on averages computed by the Bureau of Labor Statistics if no better information is available. Leach v. Commissioner, 36 T.C.M. 998, T.C. Memo. 1977-243 (1977). However, if the notice of deficiency asserts that a taxpayer has received unreported income, the IRS must prove the existence of a source of income and must provide reasonable predicate evidence for that determination. Portillo v. Commissioner, 932 F.2d 1128 (5th Cir. 1991); Weimerskirch v. Commissioner, 596 F.2d 358 (9th Cir. 1979). If the IRS has no evidence to support its determination of unreported income, the notice of deficiency is not entitled to a presumption of correctness. Senter v. Commissioner, 70 T.C.M. 54, T.C. Memo 1995-311 (1995). In such a situation, the burden of proof, *i.e.*, the burden of ultimate persuasion, shifts to the IRS. Keogh v. Commissioner, 713 F.2d 496 (9th Cir. 1986). Even though this is a collection due process case and not a more traditional deficiency-determination case, we believe that a court will follow the above rules in making determinations under I.R.C. § 6330(c)(2)(B). Therefore, the IRS will not be able to sustain the assessments at issue in this case without some predicate

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[1]I.R.C. § 7491 provides that if a taxpayer introduces credible evidence with regard to a factual issue relevant to ascertaining the taxpayer's liability, the burden of proof with respect to such issue shifts to the Commissioner. In order to take advantage of this statute, a taxpayer must meet certain conditions as described in the statute. However, this provision applies only to court proceedings arising from examinations commenced after July 22, 1998. Therefore, I.R.C. § 7491 is not applicable to this case.

evidence of a source of income. We do not believe that the rental application discussed above is, alone, sufficient to show that the taxpayer was employed by [redacted].

As we understand the facts of this case, the IRS has no documents such as Forms W-2 or Forms 1099 showing that the taxpayer received income during the years at issue. We recommend that you attempt to contact [redacted], the person noted on the rental application as being the taxpayer's employment supervisor during the years at issue. We also recommend that you ask the taxpayer detailed questions about where he lived during the years at issue, and with whom. You should attempt to contact any persons identified by the taxpayer to see if they corroborate the taxpayer's testimony. If the taxpayer's Social Security records can be obtained, they should be examined. Any relevant unemployment records that can be obtained should be examined. If investigation of these sources leads to evidence that the taxpayer did in fact receive income during the years at issue, we may be able to partially or completely defend the assessments at issue. However, if we cannot locate any evidence of a source of income during the years at issue, we will have nothing with which to contradict the taxpayer's testimony that he did not have income. Under those circumstances, we would recommend conceding the case.

Since nothing further remains to be done on this case, we are closing our file.

WILLIS B. DOUGLASS
Attorney

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